Montana Department of Revenue

EXHIBIT 4
DATE 2/17/09
HB 2

DP 20001 – Present Law Base Adjustment
Information Technology and Processing Division

Impact Statement: DP 20001 requests $296,316 over the biennium. Failure to pass this decision package impacts the state's ability to collect revenues. In the event that this decision package is not approved, revenue projections for the state will need to be reduced by $977,843.

To protect confidential taxpayer data from unauthorized disclosure, federal and state law requires the Department of Revenue to have direct control of its data. The department cannot delegate this responsibility and authority to the Department of Administration, Information Technology Services Division (DOA-ITSD). Further, failure to properly segregate taxpayer data within the state's central computer system creates risks of taxpayer data being improperly disclosed through 1) commingling with data used by other agencies or 2) accidental disclosure publicly on the Internet or through other means. In order to address this situation, the department is currently working with the DOA-ITSD to develop and implement a segregated server environment in their data center. Costs associated with the setup of the server environment will take place during FY2009.

The ongoing costs of this server environment requested in this DP include software licenses and support (Oracle), hardware maintenance and support, and miscellaneous items such as floor space and network connections in the data center itself. The general code used in MBARS (62136) is only a guide. Payment for this server environment will be made to the DOA-ITSD, not an outside contractor, for their services related to this project. The DOR and DOA have worked closely to keep the costs of this project to a minimum.

DP 7021 – Abandoned Property Program Workload Increase
Request for 2.00 FTE and Spending Authority

Impact Statement: DP 7021 requests $218,874 in State Special Revenue authority over the biennium. Passage of this decision package has a positive impact on the state's ability to collect revenues and return unclaimed property to citizens. In the event that this decision package is approved, the state's Revenue Estimate can be increased by $250,000 and estimated unclaimed property returned to citizens can be increased by $70,000.

The Department of Revenue's DP 7021 – Abandoned Property Program Workload Increase – requests 2.00 FTE to reconcile abandoned securities and mutual funds for Montanans. Currently, the department's two abandoned property auditors – who should be conducting audits to secure the reporting of more abandoned property – are instead reconciling security and mutual funds, authorizing the sale and transfer of securities and mutual funds, and approving the return of the securities and mutual funds to the rightful owners on a daily basis. This use of the auditors' time is a misallocation of resources that will result in less abandoned property being reported to the state. However, this circumstance is unavoidable due to the limited staffing for this program. The requested FTE will handle the daily reconciliation and maintenance on securities and mutual funds and allow our audit team to concentrate on audits, thus 1) increasing the amount of abandoned property returned to the state, 2) benefiting Montanans by returning more property to them, and 3) benefiting the state's general fund by increasing revenue.

Since the inception of the Abandoned Property Program in 1963, the department has received approximately $70,000,000 in abandoned property funds for Montana. Approximately $20,000,000 of these funds has been returned to their rightful owners leaving $50,000,000 in the general fund.

In the past 10 years, the amount of abandoned property returned to the state has tripled. The department currently is holding over 1,000,000 shares of stock. Between July 2007 and June 2008, over 3,100 securities related transactions occurred in the state's abandoned property account. These transactions included: securities escheated to the state; securities sold; securities reissued; dividend payments (cash and reinvesting dividends); stock splits; stock reverse splits; mergers; involuntary liquidations; and other transactions.

Each of these transactions requires the department to make the necessary adjustments to each owner's records as the transaction occurs. Without making these adjustments, owner's records do not adequately reflect the current value of their property that is held in perpetuity by the state.

The department is requesting the additional FTE to allow the auditors to conduct audits to increase audit collections. In addition to increased audit collections, a larger audit presence will increase the amount of voluntary compliance funds paid to the state.

DP 70003 – Reduce Smoking through Tobacco Tax Compliance Request for 3.00 FTE and Spending Authority

Impact Statement: DP 70003 requests $355,733 in State Special Revenue authority over the biennium. Failure to pass this decision package has a direct impact to the state's Revenue Estimates because it impacts the state's ability to collect the $93,000,000 in tobacco tax revenues and also places at risk the $25,000,000 per year in Tobacco Master Settlement Agreement payments. If this decision package is not passed, the official Revenue Estimates need to be decreased by $1,067,199.

The Department of Revenue's DP 70003 – Reduce Smoking through Tobacco Tax Compliance – requests 3.00 FTE to fund the continuation of the state's Tobacco Tax Compliance Program.

In FY2006, 3.00 modified FTE were authorized to establish a Tobacco Tax Compliance Program. The 2007 Legislature funded the program without the FTE, so modified FTE were authorized again during the 2009 biennium. This decision package requests to make the 3.00 FTE permanent. These 3.00 FTE have been full time employees since FY2006.

The program ensures tobacco tax compliance through auditing of tobacco wholesalers and retailers to ensure that all tobacco products are properly stamped and all taxes have been paid.

The audit program is responsible for the over $93,000,000 of taxes paid to Montana. This equates to each auditor being responsible for $31,000,000 of tax revenue.

The audit program also is necessary in that without an effective audit program the Tobacco Master Settlement Agreement (TMSA) funds could be at risk. Through the department's audit program, as well as the Department of Justice's enforcement activity, the TMSA payments have not been reduced. The tobacco companies have been challenging the TMSA payment if a state's enforcement is weak. The tobacco companies have been successful in delaying and/or getting out of making TMSA payments. In addition to the $93,000,000 of tobacco taxes paid annually, Montana receives about $25,000,000 in TMSA payments each year.

Without this program, the department will not have an audit program for the tobacco taxes and the smuggling of tax free tobacco will become prevalent in Montana. Without this audit program, the collection of taxes and TMSA payments will be jeopardized. Without these funding sources, essential services such as tobacco prevention and cessation, funding for Children's Health Insurance Program, and Medicaid matching funds will be at risk.

DP 9000 – Enhanced Tax Compliance to Partially Finance Business Equipment Tax Reductions Request for 10.00 FTE and Spending Authority

Impact Statement: <u>DP 9000 requests $1,617,514 over the biennium. Passage of this decision package will provide a portion of the necessary replacement revenues to provide business equipment tax reductions for small Montana business – a total of $8.6 million in the 2011 biennium. If this decision package is not passed, the ability to pass some Montana small business equipment tax reductions will be in jeopardy.</u>

The Department of Revenue's DP 9000 – Enhanced Tax Compliance to Partially Finance Business Equipment Tax Reductions – requests 10.00 FTE to ensure that all Montana taxes owed by pass-through entities are correctly reported and paid.

Non-resident owners of companies organized as pass-through entities are among the largest identifiable source of unpaid taxes to Montana. Preliminary work by 2.50 FTE over the last few years has yielded $15 for each dollar invested. There are over 45,700 pass-through businesses operating in Montana with hundreds of thousands of owners who are accountable under the law for paying taxes on this income earned by these businesses. Only 2.50 FTE are available to conduct audits in this area. In contrast, the highly productive corporate tax audit program uses 14.00 FTE – a program that has produced $33.2 million in income over the last biennium. Thus in comparison with other valuable programs, auditing of pass-through entities is woefully understaffed.

These types of compliance programs are essential to ensure the stability and health of Montana's tax system. To ensure this occurs, ongoing compliance efforts are required. The department, through this proposed staff, will identify compliance issues by taxpayer, group of taxpayer, industry, and by a specific tax issue. Once these issues are identified, the department will work with taxpayers to resolve the issue. Through the taxpayer and department's efforts, these compliance issues do get resolved.

Unfortunately, the department's experience indicates that even though the specific compliance issues may have been addressed with a taxpayer, the same or similar issues come up in future compliance work. This happens even though the department has conducted a prior audit and has provided more timely and clear tax information through tax booklets and outreach programs. Because of the repeated non-compliance, it is essential that the department appropriately staffs areas such as this to ensure the stability and health of Montanan's tax dollars.

DP 80002 – Improving Property Appraisal Accuracy
Property Assessment Division

Impact Statement: DP 80002 requests $378,841 over the biennium. This request presents an innovative approach to help forestall the size of future FTE increases due to property valuation workload. Failure to pass this decision package will result in larger FTE requests in future biennia as workload in this area continues to grow.

There are two parts to this decision package – one aimed at helping keep up with the increased property workload and the other aimed at creating a new process to improve the efficiency of the existing property valuation staff. Both proposals help keep pace with the increasing volume of property tax work.

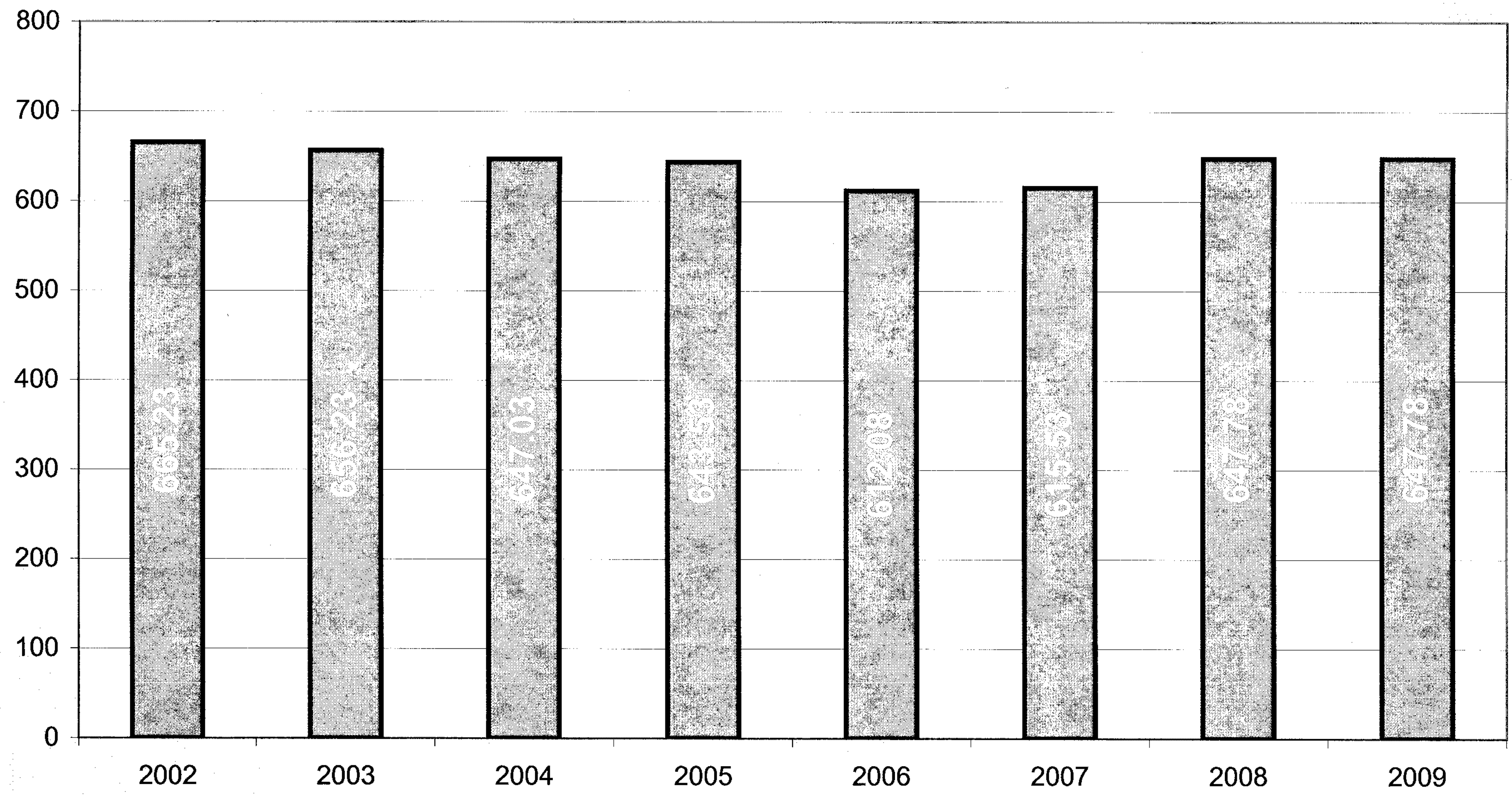
Two FTE are requested to help keep up with the close to one million parcels that are subject to reappraisal. Twenty five percent of all existing parcels must be reviewed annually as a continuous process in each new appraisal cycle. All new land use changes need to be reviewed annually. Ten thousand new construction parcels are accounted for annually and that new property then becomes a permanent addition to the property that must be reviewed in each reappraisal cycle. Therefore, new construction has both an immediate and a continuous, ongoing impact on workload.

In 1996, the department maintained 2,100 parcels per FTE.

Today that ratio is 3,100 per FTE.

To create efficiencies, the department proposes to implement a property owner self-reporting system. Under this system, the department would provide property owners with pre-populated forms describing building characteristics. The property owner can then provide feedback on changes to the characteristics. This will allow for more focused time management strategies for department staff and will improve the accuracy of the information. Costs will fund a cover letter; the self-reporting form; postage paid return envelope; a taxpayer education program; and an advertising campaign for the project.

FTE by Fiscal Year -
Department of Revenue



Prepared by the Department of Revenue